CC Docket #96-98
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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

VIA HAND DELIVERY

The Honorable William E. Kennard
Chairman
Federal Communications Commission
1919 M Street, N.W., Room 814
Washington, D.C. 20554

Re: Reciprocal Compensation for Traffic Terminating to ISPs

Dear Chairman Kennard:

This letter is submitted on behalf of WorldCom, Inc. ("WorldCom"), in response to a letter sent to you by Bell Atlantic on July 1, 1998.[1] The Commission should reject Bell Atlantic's request to declare telephone traffic, traveling from an incumbent local exchange carrier's ("ILEC") end user customers to an Internet service provider ("ISP") located within the same local calling area and served by a competitive local exchange carrier ("CLEC"), as somehow outside the obligation imposed by the Telecommunications Act of 1996 for carriers to agree contractually to provide compensation for terminating traffic. As the attached analysis explains in further detail, granting Bell Atlantic's request would nullify the requirements of the 1996 Act, destroy market-based mechanisms envisioned by Congress, intrude unnecessarily in bilateral contractual relationships, overrule unanimous state commission determinations, preempt state jurisdiction, and otherwise jeopardize competition.

Bell Atlantic's primary argument is that it is paying out too much money in reciprocal compensation payments to CLECs relative to the amount of money it collects from its own end users. Simply put, the reciprocal compensation rates that Bell Atlantic and the other ILECs voluntarily negotiated, and represented repeatedly in 1996 as both cost-based and applicable to traffic terminating to ISPs, are now too high for their liking. While seeking to cast the issue as solely one of "local versus interstate" classification, Bell Atlantic conveniently ignores the pertinent statutory, contractual, and historical context. Instead of looking forward to a return to the bargaining table with WorldCom and other CLECs as their original interconnection

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[1] Letter from Edward D. Young, III, Senior Vice President and Deputy General Counsel, Bell Atlantic, and Thomas J. Tauke, Senior Vice President, Government Relations, Bell Atlantic, to The Honorable William E. Kennard, Chairman, Federal Communications Commission, dated July 1, 1998 ("Bell Atlantic Letter").

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agreements begin to expire, however, or attempting to rationalize its local exchange rate structures, Bell Atlantic is asking that the Commission intervene in the private negotiation and state arbitration processes. What Bell Atlantic wants, in short, is a government-sponsored "bail out" of Bell Atlantic's mutually agreed-to obligations under its interconnection agreements. WorldCom urges the Commission to decline Bell Atlantic's request for such an unlawful, inequitable, and arbitrary and capricious action.

As the attached analysis explains, there is no basis for any Commission action on Bell Atlantic's request because:

- **The 1996 Act requires that carriers be compensated for the cost of terminating traffic.**

Section 252(d)(2) provides that all local carriers, including CLECs, have the right to recover the costs associated with terminating traffic from another carrier's customers.

- **The 1996 Act does not recognize different termination rates for different classes or types of end user customers.**

Nothing in the Act, FCC rules, or interconnection agreements creates any rate distinctions in terminating traffic to different types of customers.

- **The 1996 Act left the determination of specific termination charges to private contract negotiations between CLECs and ILECs.**

Section 251(b)(5) mandates that ILECs and CLECs establish binding compensation arrangements for terminating traffic, while Section 251(c)(1) and Section 252 require carriers to reach binding agreements on these and other interconnection issues through either voluntary negotiations or state arbitrations.

- **The 1996 Act left the arbitration, review, and approval of specific termination charges to individual state public service commissions.**

Section 252 gives the state commissions exclusive authority to conduct compulsory arbitration proceedings, and review and approve interconnection agreements.

- **In 1996, Bell Atlantic demanded, and received, high reciprocal compensation rates -- far above the FCC's proxy rates -- in its interconnection negotiations with MFS Communications (now part of WorldCom) and other CLECs.**

Denigrating what it called "bilk and keep" alternative as "a plea for a government handout," Bell Atlantic insisted that MFS agree to reciprocal compensation rates of up to 0.9 cents per minute, far above the FCC's proxy rates of 0.2 to 0.4 cents per minute.

- **In 1996, Bell Atlantic acknowledged to MFS, to the FCC, and to state regulators that traffic terminating to ISPs is local and is subject to reciprocal compensation.**

In particular, in a May 30, 1996 filing in CC Docket No. 96-98, Bell Atlantic asserted that any fears about ILECs seeking high reciprocal compensation rates with CLECs "reflects a fundamental misunderstanding of the market." If an ILEC sets termination rates too high, Bell Atlantic assured that CLECs "will sign up customers whose calls are predominantly inbound," including "internet access providers." Bell Atlantic intimated that, as a result, no ILEC would seek high termination rates because it "will find itself writing large monthly checks to the new entrant."

Thus, in this and other public documents, Bell Atlantic readily conceded in mid-1996 that: (1) traffic terminating to ISPs is local traffic subject to the reciprocal compensation obligation; (2) CLECs have the right to sign up ISPs as local customers; (3) the ILECs owe CLECs reciprocal compensation for traffic terminating to the CLECs' ISP customers; and (4) "the market" will ensure that terminating rates are never set too high.

- **The ILECs themselves historically have treated, tariffed, billed, declared, and reported traffic terminating to ISPs as local, and thus subject to reciprocal compensation.**

The ILECs themselves long have treated traffic to ISPs as local, which includes (1) classifying their own end user customers' calls to ISPs as local calls, (2) tariffing those calls, as local, (3) billing those calls as local, (4) declaring those calls to be local, and (5) reporting those calls as local. Indeed, it would be a flagrant violation of Section 271 of the 1996 Act for the RBOCs to provide this traffic on an interstate basis.

- **The Act is working as intended -- the contract renegotiation process, state cost proceedings, and the marketplace will take care of any perceived concerns about specific termination rates.**

In particular, Bell Atlantic has filed SGATs in several states containing reciprocal compensation rates of between 0.28 and 0.37 cents per minute, far below the per-minute rate of 0.9 cents it insisted upon in 1996, and much more in line with the FCC's own proxy rates.

- **All nineteen state commissions to address the issue thus far agree that traffic terminating to ISPs is subject to mutual reciprocal compensation obligations.**

These states are Arizona, Colorado, Connecticut, Illinois, Maryland, Michigan, Minnesota, Missouri, New York, North Carolina, Oklahoma, Oregon, Pennsylvania, Tennessee, Texas, Virginia, Washington, West Virginia, and Wyoming.

- **Relevant FCC precedent and factual analysis shows that traffic terminating to ISPs is local.**

As the FCC has concluded: (1) ISPs are end users, not carriers; (2) calls to ISPs involve two separate transmissions, one of which constitutes a local call from end users; (3) ISPs incorporate local telecommunications into their provision of information services, just like many other businesses; and (4) access charges apply only to three carriers (two LECs and an IXC), while reciprocal compensation applies to two LECs.

- **The current termination rate structure gives both ILECs and CLECs significant incentives to invest and compete in the marketplace.**

Among other things, the ILECs and CLECs both are incented to (1) bargain for lower, cost-based interconnection rates, (2) build out local facilities, (3) compete head-to-head for ISP business, and (4) deploy DSL and other broadband local services.

Further, even aside from all the important legal, policy, equity, and factual reasons why the Commission should reject Bell Atlantic's call for federal intervention in private contractual relationships, granting Bell Atlantic's request could create a fundamental sea change in current law and policy, and open up enormous new legal, policy, and political problems. In particular, the Commission would be wading into a host of new regulatory and jurisdictional questions about the precise classification of all calls within the local exchange. For example, it is likely that current end user local exchange services used to connect to ISPs would need to be reclassified as interstate, including local usage, voice grade phone lines, and basic rate ISDN lines. Local exchange services used by ISPs to connect to the network also would need to be reclassified as interstate, including basic business lines, PBX trunks, and Primary Rate Interface lines. In addition, the Commission would need to develop, implement, and enforce brand new separations rules, access charge schemes, and universal service funding mechanisms. New line drawing between telecommunications and information services also would be necessitated.

In short, the FCC should reject Bell Atlantic's baseless request to classify traffic from ILEC end user customers to CLEC ISP customers as outside the statutory and contractual obligation to provide reciprocal compensation for such traffic.

Respectfully submitted,

Catherine R. Sloan

Catherine R. Sloan
Vice President, Federal Affairs

cc: Commissioners Furchtgott-Roth, Ness, Powell, Tristani
Kathy Brown, Chief, Common Carrier Bureau

The FCC Should Reject Bell Atlantic's Attempt To Evade Its Statutory And Contractual Obligation To Compensate CLECs For Traffic Terminating to ISPs

Commission action would be procedurally suspect at this time because there is no pending proceeding at the Commission.

There is no pending proceeding on this issue at the Commission, with a complete record that is ripe for Commission action. On July 2, 1998, the Association for Local Telecommunications Services ("ALTS"), citing unanimous decisions in favor of CLECs by nineteen state public service commissions, withdrew its request for clarification of this issue in CCB/CPD 97-30.[1] WorldCom is unaware of any other proceeding in which this issue is pending.

The Act requires that CLECs be compensated for cost of terminating traffic.

The Act clearly provides that all local exchange carriers, including CLECs, have the right to recover the "costs associated with the transport and termination on each carrier's network facilities of calls that originate on each carrier's network facilities of calls that originate on the network facilities of the other carrier."[2] In turn, the Local Interconnection Order defines "termination" as the switching of traffic at the terminating carrier's end office switch and "delivery of that traffic from that switch to the called party's premises."[3] That is precisely what is occurring when ILECs pay CLECs compensation for traffic terminating to ISPs: the CLEC is rendering the service of terminating calls from the ILECs' end user customers, while the ILEC avoids incurring the costs of termination itself.

The Act does not recognize different termination rates for different classes or types of CLEC customer.

Nothing in the 1996 Act, the FCC's own rules, or the interconnection agreements contemplates class of service distinctions for reciprocal compensation. Many end users, such as telemarketers, generate primarily outbound traffic, while

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[1] Letter from Richard Metzger, Vice President and General Counsel, ALTS, to Kathryn C. Brown, Chief, Common Carrier Bureau, FCC, CC Docket No. 96-98/ CCB/CPD 97-30, filed July 2, 1998.

[2] 47 U.S.C. Section 252(d)(2)(A)(i).

[3] Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499 (1996) ("Local Interconnection Order") at para. 1040.

other end users, such as Ticketmaster, pizza delivery shops, call-in radio shows, and insurance agencies, generate primarily inbound traffic. The Commission should not attempt to create, out of whole cloth, different termination rates, or different rate structures, based upon the specific characteristics of individual end users. This type of arbitrary and capricious action would raise serious discrimination concerns under the Act.

The Act left this matter to private contract negotiations between CLECs and ILECs.

Section 251(b)(5) mandates that local exchange carriers must "establish reciprocal compensation arrangements for the transport and termination of telecommunications."[4] Section 251(c)(1) imposes on all ILECs (and CLECs) "the duty to negotiate in good faith" interconnection agreements, while Section 251(c)(2) obligates ILECs to establish interconnection "on rates, terms, and conditions that are just, reasonable, and nondiscriminatory." Section 252 establishes specific procedures for ILECs and CLECs to reach binding agreement, through either voluntary negotiations or compulsory state arbitration.

Thus, under the 1996 Act, as interpreted by the Eighth Circuit, it is crystal-clear that Congress intended the reciprocal compensation issue to be outside of federal regulation. Instead, the Act relies on private, bilateral negotiations, and (if necessary) the states as backup arbitrators, to determine the rates, terms, and conditions of interconnection. The Commission has no independent authority to "fix" contractual agreements.

The Act left this matter to state arbitration, review, and approval processes.

Section 252 establishes specific procedures for ILECs and CLECs to reach binding agreement, through either voluntary negotiations or compulsory state arbitration. State commissions are not allowed to find transport and termination rates to be just and reasonable unless they provide for the mutual and reciprocal recovery by each carrier of costs associated with transport and termination.[5] Whether the interconnection agreement is completed via negotiation or arbitration, the Act grants the state commissions exclusive authority to approve or reject those agreements.[6]

Ironically, in appealing the FCC's Local Interconnection Order, the ILECs

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[4] 47 U.S.C. Section 251(b)(5).

[5] 47 U.S.C. Section 252(d)(2).

[6] 47 U.S.C. Section 252(e)(1).

argued that the state commissions, and not the FCC, had sole authority to determine the prices for the transport and termination of calls.[7] The Eighth Circuit ultimately agreed with the ILECs, and ruled that the FCC has no jurisdictional authority to supersede the "hog tight, horse high, and bull strong" fence around the states' local turf.[8] Bell Atlantic appears to have changed its tune abruptly on this point of law.

The Commission should not interfere in the private negotiation process.

Beginning well before the 1996 Act was enacted, and continuing throughout 1996, MFS Communications, Inc. ("MFS") (now a wholly-owned subsidiary of WorldCom) commenced negotiating interconnection agreements with the ILECs. Those various agreements clearly included all local traffic to each party's local customers, and did not contain any exceptions for traffic to information service providers ("ISPs") or other classes of customer.

In order to recover the costs of terminating local calls, MFS initially proposed the establishment of bill-and-keep arrangements, whereby each carrier would bill its own customers for calls to the other carrier's customers, and retain the revenue itself. Without exception, the ILECs all rejected this approach. Bell Atlantic, for example, denigrated these requests as "a plea for a government handout" that it labelled "bilk and keep,"[9] and argued instead that CLECs must pay Bell Atlantic reciprocal compensation, with a rate identical to Bell Atlantic's own intrastate access charges. Although MFS did not agree to this approach, Bell Atlantic and the other ILECs then pressed for the payment of reciprocal compensation based on their claimed actual costs of terminating traffic to their networks. In WorldCom's estimation, the ILECs assumed that the vast majority of local traffic would terminate to their networks, so that they would reap all the benefit of high rates. WorldCom also believes that Bell Atlantic sought to influence the Commission's still-pending Local Interconnection Order and the proxy rates that the Commission might be selecting to cover the costs of terminating traffic.[10]

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[7] Iowa Utilities Board v. FCC, No. 96-3321 (8th Cir.), July 18, 1997, slip. op. at 101.

[8] Id. at 113.

[9] Reply Comments of Bell Atlantic, CC Docket No. 96-98, dated May 30, 1996, at 20 ("Bell Atlantic 96-98 Reply Comments").

[10] It is worth noting that, despite the FCC's conclusion in August 1996 that the cost-based default proxy rate for termination should approximate 0.2 to 0.4 cents per minute, the ILECs consistently insisted in prior negotiations on the establishment of reciprocal compensation rates many times higher than that cost-based range. See

Bell Atlantic's firm insistence on reciprocal compensation left MFS with few options. Because MFS was a small start-up company eager to get into the local business, and otherwise had little negotiating leverage to reject the ILECs' insistence on reciprocal compensation tied to high termination rates, MFS accepted the ILECs' position as part of its interconnection agreements. Those agreements, including the reciprocal compensation arrangement, subsequently were approved by most state commissions.

Bell Atlantic told regulators in 1996 that traffic terminating to ISPs is subject to the reciprocal compensation obligation.

Bell Atlantic's shameful attempts at revisionist history cannot succeed. There is absolutely no doubt that, at the time Bell Atlantic negotiated its interconnection agreements with MFS, and throughout all of 1996, Bell Atlantic had full knowledge of, and agreed with, the proposition that traffic terminating to ISPs was included in the reciprocal compensation obligation. Indeed, Bell Atlantic expressly acknowledged the point in comments filed with the FCC in Docket No. 96-98 in May 1996. In arguing that the Commission should reject bill and keep in favor of reciprocal compensation, Bell Atlantic stated:

> Moreover, the notion that bill and keep is necessary to prevent LECs from demanding too high a [reciprocal compensation] rate reflects a fundamental misunderstanding of the market. If these rates are set too high, the result will be that new entrants, who are in a much better position to selectively market their services, will sign up customers whose calls are predominantly inbound, such as credit card authorization centers **and internet access providers**. The LEC will find itself writing large monthly checks to the new entrant.[11]

There is further ample evidence that Bell Atlantic in 1996 readily conceded to state regulators that traffic terminating to ISPs is subject to the reciprocal compensation

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Local Interconnection Order at para. 1060. Bell Atlantic, for example, demanded a per-minute termination rate of 0.9 cents in its New Jersey, Pennsylvania, and Maryland interconnection agreements with MFS, which were signed prior to the FCC's issuance of the Local Interconnection Order.

[11] Bell Atlantic 96-98 Reply Comments, at 21 (emphasis added).

obligation.[12]

Bell Atlantic's May 1996 filing with the FCC reveals many important points which directly contradict much of the content of its July 1, 1998 letter. These points include:

(1) Bell Atlantic demanded reciprocal compensation arrangements with CLECs for terminating traffic;

(2) Bell Atlantic acknowledged that traffic terminating to "internet access providers" is local traffic;

(3) Bell Atlantic acknowledged that traffic terminating to "internet access providers" is subject to reciprocal compensation payments to CLECs;

(4) Bell Atlantic acknowledged the CLECs' right to sign up ISPs as local customers;

(5) Bell Atlantic acknowledged that it and other ILECs would owe CLECs reciprocal compensation for traffic terminating to ISPs; and

(6) Bell Atlantic believed that, if the reciprocal compensation rates were set too high by the parties, "the market" will take care of the situation because CLECs would seek out ISPs as local customers.

In other words, despite Bell Atlantic's present-day protestations, Bell Atlantic knew the truth then, and it knows the truth now.

Much as Bell Atlantic predicted in May 1996, following state approval of interconnection agreements including high reciprocal compensation rates for traffic terminating to ISPs, CLECs began to sign up ISPs as end user customers. Indeed, the ISPs actively sought out the CLECs as viable alternatives to the incumbent local carriers. In large part, the ISPs were drawn to the CLECs' better pricing, higher quality of service, more flexible collocation arrangements, and superior circuit availability.

Now, based on changing marketplace conditions, Bell Atlantic and the

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[12] See, e.g., Petition of Cox Virginia Telecom, Inc. for Enforcement of Interconnection Agreement and Arbitration Award for Reciprocal Compensation for the Termination of Local Calls to Internet Service Providers, Case No. PUC970069, filed June 10, 1997, at 14-16 (Bell Atlantic arbitration witnesses testified that calls terminating to ISPs are local and subject to reciprocal compensation under the pending interconnection agreements).

other ILECs seek unilaterally to rewrite history, and undo their bargain with CLECs, rather than compete in the marketplace. Of course, this is a not unexpected, knee-jerk reaction by monopolies long accustomed to reaping supra-competitive profits and living within the safety of regulatory paternalism. The simple fact is that Bell Atlantic made comprehensive interconnection deals with dozens of CLECs, including WorldCom, that fully reflected the intentions of the parties. Bell Atlantic now solicits the Commission's assistance in nullifying one specific aspect of those deals that is no longer to its liking.

The Commission should not kid itself; it has become the ILECs' avenue of last resort, as every state commission and federal court to consider the issue to date has ruled against the ILECs. Because the ILECs perceive that they are not getting the full one-way benefit of a piece of the bargain they struck with CLECs -- lots of incoming reciprocal compensation revenue from CLECs, with little to no revenue outlay to CLECs -- they want the ultimate regulatory intervention: a Commission rewrite of private contracts that will undo the results of several years of private negotiations and deny ISPs the choices they have made in the free marketplace. Indeed, Bell Atlantic's ulterior motive here -- as in its Section 706 petition now pending before the Commission -- is nothing less than a brazen attempt to foreclose future competition in the data services market. One can only imagine Bell Atlantic's cries of "government bail-out" and "handout" should a CLEC have sought similar FCC intervention in nullifying an interconnection agreement the CLEC signed with Bell Atlantic.

The Act is working as intended; the contract renegotiation process, state cost proceedings, and the marketplace will take care of any perceived problem.

While Bell Atlantic in its letter rails against the current rate and rate structure for traffic terminating to ISPs -- elements it insisted upon specifically in contract negotiations -- it fails to provide any evidence to suggest that the Act is not working as intended, and that the market mechanisms established by the Act are not functioning as planned. The ILECs are perfectly free to seek lower rates as part of the ordinary negotiation process for renewal of the arbitration agreements. That is precisely how the process is supposed to work under the Act. To the extent that Bell Atlantic and the other ILECs believe the reciprocal compensation rates they bargained for are now above actual cost, they can rectify that situation through future negotiations with CLECs when the current interconnection agreements expire. In fact, many of those agreements currently are being renegotiated.[13]

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[13] At least one ILEC apparently has told regulators that most favored nation ("MFN") provisions in current interconnection agreements will preclude the ILECs from addressing the reciprocal compensation issue. However, this directly contradicts the

Moreover, Bell Atlantic and the other ILECs can look to the states as well.[14] In many states, ongoing cost proceedings are establishing lower rates for reciprocal compensation than those insisted on earlier by the ILECs. The ILECs also have begun to file in various states their updated statements of generally available terms ("SGATs"). In most cases, those SGATs contain far lower reciprocal compensation rates, sometimes even below the FCC's proxy rates. For example, even though Bell Atlantic demanded reciprocal compensation rates of 0.9 cents per minute in its 1996 interconnection agreements with MFS, Bell Atlantic's recent SGAT filings in New Jersey, Pennsylvania, and Maryland contain per-minute reciprocal compensation rates of 0.37 cents, 0.28 cents, and 0.33 cents, respectively. Apparently Bell Atlantic now believes that its cost structure has decreased in those states to such an extent that the termination rates it was obligated to negotiate in good faith no longer are an accurate reflection of its true costs.

In short, the market currently is working as Congress intended. There is no need for the Commission to intrude into the process in an arbitrary and capricious manner.

Granting Bell Atlantic's request would have direct anticompetitive market consequences.

Any Commission action at this time would amount to blatant interference in the statutorily-guarded private negotiation process between ILECs and CLECs. In particular, by removing one of the CLECs' primary sources of bargaining leverage in future negotiations, the Commission would be giving the ILECs a major, unilateral rewrite of their interconnection agreements. As a result, the CLECs would be unable to trade that concession for other pro-competitive concessions, such as lower loop rates or improved collocation arrangements. Moreover, the ILECs no longer would be under any pressure to significantly lower their reciprocal compensation rates for all local traffic, not just calls to ISPs, so that CLECs will continue to pay ILECs high rates

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ILECs' own position in the states that those MFN provisions only remain in effect so long as the underlying contract itself remains in effect. Thus, under the ILECs' own reasoning, once the original contract expires, so does the MFN provision.

[14] Indeed, in the Access Reform Order, the FCC directed the ILECs to turn to state commissions in very similar circumstances. There, the FCC found that, "[t]o the extent that some intrastate rate structures fail to compensate incumbent LECs adequately for providing service to customers with high volumes of incoming calls, incumbent LECs may address their concerns to state regulators." Access Charge Reform, CC Docket No. 96-262, First Report and Order, 12 FCC Rcd 15982 (1997) ("Access Charge Reform Order") at para. 346.

to terminate all other local traffic. The Commission also would be putting its official imprimatur on the notion that ILECs are free to use the CLECs' local networks without any obligation to pay for that usage.

The states can take enforcement action against any individual CLEC violating the Act.

In its July 1 letter, Bell Atlantic complains about "illicit" conduct "bordering on fraud" by unnamed CLECs, by which ISPs allegedly seek CLEC status in order to receive reciprocal compensation.[15] Nonetheless, the letter provides absolutely no evidence of the type of activity that Bell Atlantic claims is so rampant. WorldCom doubts that such conduct, if it even exists, poses anything like the threat that Bell Atlantic alleges. Of course, Bell Atlantic is perfectly free to file its claims with the state public service commissions, which the Act entrusts with the role of certifying and policing CLECs, and enforcing interconnection agreements. The fact that Bell Atlantic apparently has not done so betrays the lack of credibility in its claims. Indeed, even if these allegations have any merit, complete elimination of all reciprocal compensation obligations for traffic terminating to ISPs would be a decidedly out-of-proportion response by the Commission. Any such activities also would pale in comparison to the ILECs' continuing attempts to avoid paying all outstanding reciprocal compensation owed to CLECs.

All state commissions and federal courts unanimously agree that traffic terminating to ISPs is subject to reciprocal compensation.

Importantly, all nineteen state public service commissions to date which have reviewed the matter have concluded that traffic terminating to ISPs is subject to reciprocal compensation. Despite Bell Atlantic's assertions, those decisions largely are based not on FCC precedent, but rather on (1) interpretation of specific language in specific interconnection agreements, and (2) standard ILEC and CLEC industry practice.

Further, to date, all federal courts that have reviewed the state commission decisions have concluded that traffic terminating to ISPs is subject to reciprocal compensation. Most recently, the Western District Court of Texas concluded that ILEC traffic terminating to a CLEC's ISP customer is local traffic subject to reciprocal compensation obligations.[16]

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[15] Bell Atlantic Letter at 2-3.

[16] Southwestern Bell Telephone Co. v. Public Utility Commission of Texas, No. MO-98-CA-043 (W.D. Texas, June 16, 1998).

Relevant FCC precedent demonstrates that traffic terminating to ISPs is local.

An unbroken string of Commission precedents hold that traffic terminating to ISPs is not toll telephone or exchange access service, and therefore must be local traffic.

In its Local Interconnection Order, the FCC confirmed that, under the 1996 Act, all carriers can obtain interconnection to terminate calls.[17] As explained above, the FCC defined the term "termination" to include calls to the "called party's premises."[18] Obviously, since the ISP's point of presence constitutes the "called party's premises," termination by definition includes ISPs.

The Commission also has touched on the local nature of calls to ISPs, versus the interstate nature of ISP transmissions to the Internet. Back in 1989, the Commission reiterated the long-recognized conclusion that "ESP traffic over local business lines is classified as local traffic for separations purposes," so that "[traffic sensitive] costs associated with ESP traffic are apportioned to the intrastate jurisdiction, and are recovered through intrastate charges paid by ESPs and other purchasers of intrastate services."[19]

More recently, in the Non-Accounting Safeguards Order, the FCC observed that even though an end user might obtain access via an ISP to an information service across LATA boundaries, the service is not deemed interLATA.[20] Indeed, the RBOCs argued that they are able to provide intraLATA Internet access service where the customer connects to the ISP point of presence ("POP").[21] The Commission acknowledged that two separate transmissions are involved when an end user seeks access to the Internet. First, the end user obtains access to the ISP by

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[17] Local Interconnection Order at para. 90.

[18] Local Interconnection Order at para. 1034.

[19] Amendments of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture, Notice of Proposed Rulemaking, 4 FCC Rcd 3983, 3987-88 (1989).

[20] Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended, CC Docket No. 96-149, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 21905 (1996) ("Non-Accounting Safeguards Order") at para. 119.

[21] Non-Accounting Safeguards Order at para. 126. Of course, if the Commission does determine that traffic terminating to ISPs is interstate, the RBOCs have been flagrantly violating Section 271 of the 1996 Act from day one.

using dial-up or dedicated access to the ISP's processor or platform; second, the ISP, in turn, acts as the buffer between the end user and various repositories of information content, including the Internet.[22] Similarly, in the Universal Service Order, the Commission discussed how an ISP subscriber "obtains a connection to an Internet service provider via voice grade access to the public switched network."[23] The FCC stated that "that connection is a telecommunications service and is distinguishable from the Internet service provider's service offering."[24]

The Commission also has addressed the mutually exclusive nature of reciprocal compensation and access charge arrangements. Most recently, in its report to Congress earlier this year on universal service issues, the Commission reminded Congress that access charges only apply in the long distance setting, where there are three carriers. In contrast, the FCC stated that the reciprocal compensation obligation applies only where there are two carriers, in the local exchange setting.[25] There is no doubt under law that ISPs are merely end users, not carriers, and that the ILEC and the CLEC are the only two carriers involved in terminating traffic to ISPs. Thus, pursuant to the FCC's own April 1998 analysis, reciprocal compensation must apply to such traffic.

The FCC further informed Congress that ISPs purchase thousands of local business lines in order to provide connectivity to their users; those ISPs pay state tariffed rates, subscriber line charges, and presubscribed interexchange carrier charges.[26] Of course, all of those charges apply to local lines. The Commission also found that "at least 87% of the U.S. population has access to a commercial Internet service provider through **a local call**," and "three-quarters of Americans live in **local calling areas** with at least three Internet service provider points of presence."[27] The Commission's words speak for themselves.

Bell Atlantic and other ILECs apparently believe that, because ISPs are

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[22] Non-Accounting Safeguards Order at para. 127 n.291.

[23] Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776 (1997) ("Universal Service Order") at para. 789.

[24] Id.

[25] Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Report to Congress, issued April 10, 1998 ("Universal Service Report to Congress") at para. 33.

[26] Universal Service Report to Congress at para. 97.

[27] Universal Service Report to Congress at para. 103 (emphasis added).

engaged in interstate commerce, ISP traffic must be jurisdictionally interstate. However, there simply is no connection between these two classifications. The Commission declared enhanced service providers ("ESPs") to be engaged in interstate commerce in 1982,[28] a decision later upheld by the D.C. Circuit.[29] The FCC's Computer II decision enabled it to foreclose state regulation of ESPs. At that same time, the Commission declared enhanced service providers to be end users, not carriers.[30] These seminal decisions were the governing regulatory structure of the industry until 1996, when Congress embraced them in the Telecommunications Act of 1996. Now, it is the "law of the land" that ISPs (of which ESPs are a subset) are not communications common carriers. Rather, they remain end users which incorporate telecommunication services into the provision of separate information services. Like any other end user, they may utilize any combination of telecommunication services to conduct their own business, including business as a non-common carrier provider of information services.

Factual precedent shows that traffic terminating to ISPs is local.

Of course, one of the many ironies raised by Bell Atlantic's letter is the simple fact that the ILECs themselves always have considered traffic terminating to ISPs to be local. Indeed, the ILECs' current argument about paying reciprocal compensation for traffic to ISPs flies directly in the face of the ILECs' own treatment of such traffic. The ILECs, including Bell Atlantic, (1) treat their own end user customers' calls to their ISP customers as local calls, (2) tariff those calls as local, (3) bill those calls as local, (4) declare those calls to be local,[31] and (5) report those calls as local. To WorldCom's knowledge, Bell Atlantic has never charged long distance fees to its own end user customers seeking to access a Bell Atlantic ISP.

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[28] Amendment of Section 64.702 of the Commission's Rules and Regulations (Computer II), 77 FCC 2d 384 (1980).

[29] Computer and Communications Industry Association vs. FCC, 693 F.2d 198 (D.C. Cir. 1982), cert. denied, 461 U.S. 938 (1983).

[30] 47 C.F.R. Section 64.702(a).

[31] Earlier this year, SBC notified the Commission that, effective calendar year 1997, it had begun unilaterally to classify and report traffic terminating to ISPs as interstate for separations purposes. See Letter from B. Jeannie Fry, Director, Federal Affairs, SBC, to Ken Moran, Chief, Accounting and Audits Division, FCC, dated January 20, 1998, at 1. Obviously, in announcing such a change in jurisdictional classification, SBC was obliged to acknowledge that under its longstanding practice prior to 1997, "ISP traffic was originally identified as intrastate (local) for separations and reporting purposes, instead of interstate...." Id. at 2.

Indeed, under the current interLATA restriction contained in Section 271 of the 1996 Act, Bell Atlantic would be prohibited from carrying such traffic on an interstate basis.[32] As a separate matter, WorldCom already has pointed out to the Commission that Bell Atlantic and the other RBOCs appear to be providing Internet access service in violation of the 1996 Act. Pending before the Commission since July 1996 is a petition for reconsideration filed by MFS challenging the Common Carrier Bureau's grant of a CEI plan for Bell Atlantic's Internet access service.[33] MFS explained that Bell Atlantic's CEI plan violates Sections 271 and 272 of the 1996 Act by offering bundled, in-region interLATA information services without receiving Section 271 authorization.[34] If the Commission ultimately enforces the Act by granting MFS' petition, Bell Atlantic and any other offending RBOCs will be compelled to cease their unlawful activities.

In addition, the ILECs have routinely billed WorldCom reciprocal compensation for calls terminating to the ILECs' ISP customers. Further, as explained above, Bell Atlantic acknowledged to federal and state regulators in 1996 its firm belief that calls terminating to ISPs are local calls subject to the reciprocal compensation obligation. Apparently the ILECs themselves are supposed to be all but immune from the effects of the regulatory theories they spin.

The ILECs' own historic treatment of ISP traffic is not surprising because it accurately reflects its local nature. ISPs use a wide variety of telecommunication services in their provision of information services. In particular, ISPs subscribe to local services so that their customers, who also subscribe to local services, may make a local call to the ISP. ISPs also use other dedicated or switched services to connect their various local points of presence to each other and to other ISPs. Some ISPs provide toll-free access using 800 services rather than local services. Further, any ISP could use the same access services as do common carriers -- if they so choose.[35]

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[32] 47 U.S.C. Section 271.

[33] Petition for Reconsideration of MFS Communications Company, Inc. CCBPol 96-09, filed July 3, 1996; see Bell Atlantic Telephone Companies' Offer of Comparably Efficient Interconnection to Providers of Internet Access Services, Order, 11 FCC Rcd 6919 (CCB June 6, 1996).

[34] The FCC's Non-Accounting Safeguards Order subsequently validated MFS' reading of those provisions as prohibiting the RBOCs from providing interLATA Internet access service on a bundled basis, but indicated that the lawfulness of Bell Atlantic's Internet access service was better considered in Bell Atlantic's pending CEI proceeding. Non-Accounting Safeguards Order at para. 127.

[35] Of course, the Commission only has jurisdiction over interstate common carriers, not intrastate end users.

A dial-up connection to the Internet involves two separate transmissions. First, the end user customer dials a local seven-digit telephone number to connect to the ISP platform; this telephone call constitutes local telecommunications. Second, the ISP responds to the end user's request for access to information content, including such content from the Internet or elsewhere (such as a locally-based ISP, database, or cache); this second transmission is launched by the ISP, likely over a jurisdictional private line service, to retrieve the information requested by its customers.

The initial call from the end user customer to the ISP is no different from a call to a local insurance company, newspaper sports desk, or airlines reservation counter, all of which can (and do) employ interstate telecommunications services to serve their clientele. The Commission has acknowledged this similarity as well, stating in the Access Charge Reform Order that, given "the evolution in ISP technologies and markets" since the early 1980s, and the existence of "Commercial Internet access," "many of the characteristics of ISP traffic (such as large numbers of incoming calls to Internet service providers) may be shared by other classes of business customers."[36]

The current rate structure gives the ILECs proper economic incentives to invest and compete.

Allowing the market to deal with the currently-negotiated reciprocal compensation rates will promote both local exchange competition and affordable Internet access by giving the ILECs the proper economic incentives to meet the CLECs head-on in the competitive marketplace, rather than in endless regulatory battles. First, the current rate structure gives the ILECs every incentive to negotiate cost-based reciprocal compensation rates without unnecessary regulatory intervention. Second, the current rate structure forces the ILECs to compete vigorously for ISP traffic, both by offering superior service to ISP customers and by developing their own ISP business. If an ILEC then wins ISP business away from the CLECs, that traffic is no longer subject to the reciprocal compensation obligation. Third, the current rate structure incents the ILECs to offer broadband local services, such as xDSL, which will not generate these types of reciprocal compensation charges. Even a cursory glance at the newspapers, or the ILECs' web sites, reveals that DSL deployment already is proceeding at a breakneck pace in response to consumer demand and emerging competition. Finally, the current rate structure has had the short-term effect of relieving ILECs of the need to engage in significant and costly switching upgrades to support ISPs, thereby easing local network congestion.

In contrast, bailing out the ILECs from their contractual commitments will provide the ILECs with all the wrong incentives. First, the ILECs once again will argue

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[36] Access Charge Reform Order at para. 345.

for high reciprocal compensation rates for non-ISP traffic, requiring further regulatory intervention and litigation. Second, the ILECs will be able to foreclose data competition, and monopolize that market, by eliminating the CLECs' economic ability to provide service to ISPs and their customers. Third, the ILECs will slow their development of broadband XDSL services, as dial-up access will become much more profitable to them. Fourth, when ISPs have no choice but to return to the ILECs' networks, the ILECs will reignite their "network congestion" claims as a further excuse for the imposition of interstate access charges and other regulatory measures on ISPs. In competitive markets, it is not the FCC's role to prop up any carrier with guaranteed revenue streams.

Treating traffic terminating to ISPs as local gives the CLECs proper economic incentives to invest and compete.

In a desperate attempt to shift the equities in its favor, Bell Atlantic's letter is loaded with completely unfounded and often ludicrous assertions about CLECs. Contrary to these assertions, reciprocal compensation to CLECs for transport and termination of local calls to ISPs is not "risk-free cash" or a "windfall" that amounts to "money for nothing."[37] ISPs purchase local exchange services from CLECs just like any other end user. To terminate a call to an ISP, a CLEC must utilize real interconnection facilities, real switches, and real loop facilities. Contrary to Bell Atlantic's baseless claims, the current rate structure allows CLECs to receive reciprocal compensation to recover their legitimate costs of termination, as the Act contemplates.

Moreover, the current rate structure gives the CLECs solid incentives to invest and compete in the local market. As a result of the ILECs paying reciprocal compensation for the costs they incur, the CLECs are able to continue investing their precious capital in further expansion of facilities-based networks and services. In addition, because the ILEC will be rolling out DSL and other advanced data access services in order to appear more attractive to ISPs, CLECs will have every reason to provide competing DSL services in order to retain or win ISP business.

Consumers benefit from preservation of the contract negotiation process.

Consumers are the ultimate beneficiary of the current rate structure. First, because ISPs have signed deals with CLECs based on lower rates and superior service, the customer consequently can receive lower prices from the ISP. Second, allowing ILECs and CLECs to negotiate bilaterally over reciprocal compensation and

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[37] Bell Atlantic Letter at 2.

other issues should mean lower, cost-based rates overall, which would be passed along to all consumers. Third, as indicated above, the current rate structure incents both the ILECs and the CLECs to accelerate their deployment of advanced data services such as DSL; consumers obviously will enjoy the resulting benefits of using those services. Fourth, because the ILECs claim that ISPs have caused significant congestion on their circuit-switched networks, allowing ISPs to choose to utilize CLECs instead should help relieve this claimed congestion, benefiting the ILECs' end user customers in the process.